

**Audit Guidelines for Use by
Independent Auditors in the Examination of
Foundation Grants**

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A. Background

The Inter-American Foundation (the Foundation), a U.S. government corporation, was established pursuant to part IV of the Foreign Assistance Act of 1969 (22 U.S.C. 290f(a)). The Foundation provides financial support through grant or loan programs to local organizations in Latin America and the Caribbean for self-help development projects designed to improve the social and economic conditions of the people.

The Foundation is governed by a nine member Board of Directors, each appointed by the President of the United States of America, and confirmed by the Senate for six-year terms. Under the Foreign Assistance Act, six board members are from the private sector, and three are officials or employees of U.S. Government agencies concerned with the Inter-American affairs.

The Foundation as an interested investing partner in the development effort has the need to be assured that resources provided are being effectively used toward advancement of the project in accordance with the understanding reached in the grant agreement. The Foundation believes that this need can be best satisfied for itself, the Grantee, and other parties concerned through an audit performed by an independent auditor.

Purpose and Scope

The purpose of this guideline is to give the independent auditor a general direction into the areas wherein examination is required, and guidance into other phases of the audit such as sampling, transaction testing and reporting.

1. This program is intended, in part, to provide a logical sequence to the audit effort and to reflect a mutual understanding between the independent auditors and the Foundation as to the scope required meeting Government Auditing and Reporting Standards issued by the Comptroller General of the United States. This program does not replace individual professional auditor judgement. The audit steps are intended to be of general guidance and should be expanded or modified as necessary to fit the current audit requirements.

2. The auditor is expected to exercise professional judgment, considering vulnerability and materiality, in determining the scope of audit. Transaction testing must be completed to ensure that adequate substantive testing has been done to provide a reasonable basis for an opinion. Transaction testing should be performed based upon the data obtained in the analytical procedures and the results of risk assessment. The auditor must include audit steps and procedures to provide a reasonable assurance of detecting errors, irregularities, abuse or illegal acts that are material.
3. These audit guidelines are to assist the independent auditors in the determination of compliance with grant agreement requirements. Identify and recommend changes and corrections to Grantee's systems and procedures to ensure compliance with the grant agreement requirements, laws and regulations.

The major objectives of this audit program are to:

- Assure that resources provided are being effectively used;
- Determine the extent to which the desired results or benefits established are being achieved;
- Determine the effectiveness of the organizations, programs, activities and function;
- Determine whether the Grantee has complied with the requirements of the grant agreement and laws and regulations applicable to the program;
- Identify factors inhibiting satisfactory performance;
- Identify ways of making programs work better;
- Provide a uniform model for reporting by independent auditors;
- Assess whether the objectives or proposed, new or on going programs are proper, suitable or relevant based on grant agreement terms and conditions;
- Provide guidance for consistency in areas of audit such as transaction testing, sampling, observations and reporting;
- Provide the independent auditors with direction relative to areas where audit and analysis is required by the Foundation;

- Establish consistent use of Generally Accepted Government Auditing Standards (GAGAS) and Generally Accepted Auditing Standards (GAAS) by independent auditors; and
- Establish consistency in reporting of contractual and financial information and data in accordance with Generally Accepted Government Auditing Standards (GAGAS) and Generally Accepted Accounting Principles (GAAP).

These audits have a combination of “financial” and “performance” audit objectives. Because of the interest in both financial and performance, these audits are commonly referred to as “grant audits”.

Performance audits include audits for economy, efficiency and program. Program audits generally include determining the extent to which the desired results or benefits established by the Foundation are being achieved; the effectiveness of the organizations, programs, activities, or functions and whether the Grantee has complied with the requirements of the grant agreement and laws and regulations applicable to the program.

B: Authority for Audit and Review of Audit Work

The authority for the independent auditor’s audit of the Grantee’s financial documentation, records, purchase of supplies and equipment and other inquiries related to the use of project resources is established in the grant agreement. The grant agreement also provides a means for the Foundation to see that the audit work performed under the guidelines was accomplished in a satisfactory manner.

Workpapers and related supporting documentation evidencing the independent auditor’s work to support the audit conclusions shall be subject to review by the Foundation upon reasonable notification to the independent auditors.

C: Communication with Foundation

In the event that the independent auditor has questions relative to the audit guidelines, the accomplishment of the audit program, reporting phases, audit issues, or any other condition, a need to coordinate with the Foundation Auditor may be preferred. Such coordination is encouraged, as it may be essential to the satisfactory accomplishment of the audit.

Where possible, the independent auditor should resolve any questions with the Foundation’s auditor prior to the completion of the audit fieldwork in order to minimize revisits to the Grantee. The Foundation’s auditor may be contacted either by telephone, letter (depending on the urgency), e-mail or FAX.

During performance of the audit, if a significant adverse condition is found which in the independent auditor's professional judgement needs immediate reporting, he or she should notify the Foundation's auditor or provide the facts and circumstances in a letter, as appropriate.

Examples of significant adverse conditions include but not limited to the:

- inability of the auditor to trace the Foundation's payments into the accounts of the Grantee;
- misapplications of funds contrary to the stated purpose of the agreement or the use of funds provisions of the agreement;
- substantial amount of grant funds in the hands of the Grantee not being utilized (excess funds);
- suspected fraud. The reporting of this fact to the Foundation's auditor does not preclude the independent auditor from including such finding of the conditions in the normal audit report;
- Conflict of interest between the Grantee and the In-Country Service Provider (ICS); and
- any other issue that may be deemed material by the independent auditors.

The address and telephone number of the Foundation's auditor is:

Inter-American Foundation
Attn: A. G. Garza, Auditor
901 N. Stuart Street, 10th Floor
Arlington, VA 22203

Telephone: (703) 306-4355
FAX No. (703) 306-4371

D. **Government Auditing Standards**

The Foundation requires that independent auditors comply with the audit standards established by the Comptroller General of the United States for audits of governmental organizations, programs, activities and functions. These generally accepted government auditing standards (GAGAS) should include, as a minimum, the following standards:

1. **General Standards** - These standards apply to all audit organizations, both government and nongovernment (e.g. public accounting firms and consulting firms), conducting government audits unless otherwise excluded in the general standards.
 - (a) **Qualifications** – The staff assigned to conduct the audit should collectively possess adequate professional proficiency for the task required. This standard places the responsibility on the audit organization to ensure that the audit is conducted by staff who collectively has the knowledge and skills necessary for the audit to be conducted.
 - (b) **Independence** – In all matters relating to the audit work, the audit organization and the individual auditors, whether government or public, should be free from personal and external impairments to independence, should be organizationally independent and should maintain an independent attitude and appearance.
 - (c) **Due Professional Care** – Due professional care should be used in conducting the audit and in preparing related reports. This standards places responsibility on the auditor and the audit organization to follow all applicable standards in conducting government audits. Exercising due professional care means using sound judgement in establishing the scope, selecting the methodology, and choosing tests and procedures for the audit.
 - (d) **Quality Control** – Audit organizations conducting government audits should have an appropriate internal quality control system in place and participate in an external quality control review program, if applicable. The internal quality control system established by the audit organization should provide reasonable assurance that:
 - Has established, and is following adequate audit policies and procedures; and
 - Has adopted, and is following applicable auditing standards.

These general standards relate to the qualifications of the staff, the audit organization's and the individual auditor's independence, the exercise of due professional care in conducting the audit and in preparing related reports, and the presence of quality controls.

2. **Fieldwork Standards** - Generally Accepted Government Audit Standards (GAGAS) should be used in the audit process. GAGAS, in the performance of program audits include:

- (a) **Planning**: Work is to be adequately planned.
- (b) **Supervision**: Staff are to be properly supervised.
- (c) **Legal and Regulatory Requirements**: An assessment is to be made of compliance with applicable requirements of law and regulations when necessary to satisfy the audit objectives.
- (d) **Internal Controls**: An assessment should be made of applicable internal controls when necessary to satisfy the audit objective.
- (e) **Evidence**: Sufficient competent, and relevant evidence is to be obtained to afford reasonable basis for the auditor's judgement and conclusions regarding the organization, program, activity or function under audit. A record of the auditor's work is to be retained in the form of working papers. Working papers may include tapes, films, discs, etc.

3. **Reporting Standards for Audits** - For reporting purposes, audit reports should, at a minimum, include:

- (a) **Form**:

Written audit reports are to be prepared communicating the results of each government audit.

- (b) **Timeliness**:

Reports are to be issued promptly so as to make information available for timely use by management of the Foundation.

Reports should be submitted to arrive at the Foundation no later than sixty days after the requested audit start date.

(c) Report Contents:

- Objective, Scope and Methodology – the report should include a statement of the audit objectives and a description of the audit scope and methodology.
- Audit findings and Conclusions – The report should include a full discussion of the audit findings, and where applicable the auditor's conclusion.
- Cause and Recommendations – The report should include the cause of the problem areas noted in the audit, and recommendations to correct the problem areas and to improve operations, when called for by the audit objectives.
- Statement of Auditing Standards – The report should include a statement that the audit was made in accordance with generally accepted government auditing standards (GAGAS) and disclose when applicable standards were not followed. If other auditing standards were also used, those auditing standards should be cited. For example, Generally Accepted Auditing Standards (GAAS) as prescribed by the American Institute of Certified Public Accountants (AICPA), etc.
- Internal Controls – the report should identify the significant internal controls that were assessed, the scope of the auditor's assessment work, and any significant weakness found during the audit.
- Compliance with Laws and Regulations – The report should include all significant instances of noncompliance and abuse and all indications or instances of illegal acts that could result in criminal prosecution that were found during or in connection with the audit.
- Views of Responsible Officials – The report should include the pertinent views of the responsible officials of the organization, program activity, or function audited concerning the auditor's findings, conclusions, and recommendations, and what corrective action is planned.

- Noteworthy Accomplishments – The report should include a description of any significant accomplishments, particularly when management improvements in one area may be applicable elsewhere.
 - Issues Needing Further Study – The report should include a listing of any significant issues needing further study and consideration.
 - Privileged and Confidential Information – The report should include a statement about any pertinent information that was omitted because it is deemed privileged or confidential. The nature of such information should be described and the basis under which it is withheld should be stated. For example, a Grantee may refuse to provide certain data because the Grantee claims that it is privileged and confidential. This may be a result of the Grantee attempting to reduce or impact the scope of audit.
4. **Report Presentation** - The report should be complete, accurate, objective, and convincing, and be as clear and concise as the subject matter permits.

(a) **Report Distribution**

Final audit report is to be typewritten in English and the language of the country in which the Grantee is located. **Two English language copies and one copy in the local language should be submitted to the Foundation** within the time specified in the agreement.

E. **Audit and Reporting Standards and Procedures**

Major objectives of this audit are to obtain verification of compliance with the requirements of the grant agreement between the Grantee and the Inter-American Foundation.

(1) **Control Environment**

Obtain a sufficient understanding of the Grantee's *Control Environment and Overall Accounting Controls*, including both manual and computerized activities to plan related grant audit effort. Control environment has pervasive influence on the way business activities are structure, objectives established and risk assessed. It may influence control activities, information and communications systems and monitoring activities. Control environment factors include:

- (a) integrity and ethical values;
- (b) Board of Directors or audit committee participation;
- (c) Management philosophy and operating style;
- (d) Organizational structure;
- (e) Assignment of authority and responsibility
- (f) Control environment sets the tone of an organization, influencing the control consciousness of its people. It is the foundation for all other components of internal control, providing discipline and structure.

This process requires that the auditor assess the adequacy of the Grantee's accounting policies and procedures and if they are working effectively.

(2) Accounting System

Obtain a sufficient understanding of the Grantee's accounting system. The accounting system should consist of methods and records established to identify, assemble, analyze, classify and record and report an entities transactions and to maintain accountability for the related assets and liabilities. The accounting system should be well designed to provide reliable accounting data and prevent misstatements that would otherwise occur.

Test the operational effectiveness of the Accounting Systems internal controls.

Document the understanding of the Control Environment and the Overall Accounting Controls in the independent auditor's working papers;

3. Control Risk

Assess control risk as a basis of identifying factors relevant to the design of substantive tests. Control risk is the probability that the Grantee's internal controls will not prevent or detect a material error, irregularity, or misstatement in a timely manner. In assessing control risk, the auditor should consider the effectiveness of established control activities to accomplish stated control objectives. The more effective the control activities, the lower the control risk. For example, if the auditor concludes that the relevant internal controls do not exist or that other related audits could be more efficiently performed by expanding substantive testing, then control risk should be assessed at the maximum (high).

Internal control - Report on the understanding of the internal control structure and assessment of control risk and the adequacy of the system of internal control.

4. Entrance Conference

The independent auditor shall request a brief entrance conference with a senior official (preferably the signer of the grant agreement). The independent auditor should notify the Grantee several weeks in advance before starting the audit and set up an entrance conference. This notice may be oral or in writing as appropriate. At the entrance conference, the independent auditor shall:

- (a) Request the cooperation of the Grantee and the Grantee's top management and functional area management to expedite the audit.
- (b) Give the Grantee management personnel an opportunity to explain how they have discharged their responsibilities to establish and maintain adequate internal accounting and administrative control in the review areas.
- (c) Request the Grantee to identify all reports and analysis used by any management level to evaluate and control the effectiveness, economy and efficiency of the review areas.
- (d) Request the Grantee to provide informational briefing on the organization and operations involved in the area to reduce the review time. Such briefings may cover organizational/functional assignments affecting the audit areas; system descriptions and/or flowcharts of transaction flows and systems control.
- (e) Invite the Grantee to participate actively in the review/audit.

- (f) Explain in advance the Foundation's procedures for submitting draft statements of conditions and recommendations, and establish time frames for the Grantee's response.
- (g) Explain that the scope of audit will include the overall financial administration as represented in the grant agreement.
- (h) Advise the Grantee that the audit, in part, is to assist him/her in defining and resolving any problems he/she may have encountered in the financial administration of the agreement.

5. Significant Issues – Technical Standards

It is appropriate at this point to briefly discuss the technical standards, which are important for the proper identification of significant issues and reportable condition and recommendation for corrective action to, which is included in the report to the Foundation.

Significant issues may result with a qualified audit report. Examples of significant issues include but not limited to:

- inadequate accounting and internal controls;
- inadequate and or unauthorized use of funds or resources as provided by the grant agreement;
- noncompliance with financial obligations for accomplishing the agreed upon services;
- conflict of interests between the Grantee and the In-Country Service Provider (ICS); and
- lack of supporting documentation.

Significant issues may vary ranging from simple noncompliance matters required by the grant agreement to complex issues such as mismanagement of resources provided. Both simple and complex issues should meet the following technical standard when presented in draft statements to the Grantee and in the final audit report to the Foundation.

(a) Sufficient Factual Data

During the audit process, the auditor should have obtained sufficient data to support conclusions and the need for management concerns. The auditor should include sufficient details on the nature and extent of the efficiency. Statements such as “We noted questionable expenditures...” are vague and not acceptable.

(b) Cause for Condition

Where possible, the auditor should determine the cause for the condition needing improvement.

(c) Recommendations

The auditor should include appropriate recommendations on the corrective action required by the Grantee to improve or correct the noncompliance. Recommendations on controversial matters should include that the Grantee and the Foundation’s auditor discuss the issue and reach an agreement.

(d) Responses

Where appropriate, the independent auditor should include any responses provided by the Grantee on significant issues reported.

6. Reporting Standard and Procedures

(a) Reporting Standards

The audit report should contain reliable and complete statements or significant issues (as discussed above); the position of the Grantee (whether there is agreement or disagreement); and the plan of action to be taken by the Grantee to correct each condition when he agrees with the condition reported.

If the Grantee does not agree with the conditions reported and plans no corrective action, the Grantee’s specific reasons should be included in the audit report. If in the opinion of the independent auditor, that reportable condition still exists, the independent auditor should explain why he/she believes the condition exists in rebuttal to the Grantee’s reason.

(b) The Audit Report

The audit report should be submitted to the Foundation within the time specified in the contract agreement. The audit report shall be comprised of a cover sheet, index, and applicable sections and Appendices (listed below). See Section G for a sample of an audit report format. The report should be submitted to the Foundation in 8 1/2 x 11-size paper. THE AUDIT REPORT SHOULD NOT INCLUDE OR HAVE ATTACHED BOWS, RIBBONS, GLUE, OR METAL FASTENERS, ETC. A staple at the upper left corner is sufficient.

- Cover and Index.
- Subject of Audit
- Executive Summary
- Scope of Audit
- Results of Audit
- Grantee's Organization and Systems
- Appendices

F. Audit Program

1. Purpose/Scope

- (a) This program is intended to provide a logical sequence to the audit effort and to reflect a mutual understanding between the Foundation and the independent auditor as to the scope required meeting the auditing standards and the Foundations objectives. The audit steps in the program are intended as guidance and should be expanded or eliminated as necessary to fit the current audit requirements. Those steps not required should be marked "not applicable"(N/A).

The purpose of this audit program is to give the independent auditors guidelines and direction in the scope of audit and examination required **to determine whether the Grantee is in compliance with the requirements of the grant agreement and effectively obtaining, controlling, and using resources in accordance with the requirements of the grant agreement.** Additionally, the purpose of the audit program is to determine whether costs incurred in the performance of the grant agreement are reasonable, allowable and allocable in accordance with the grant agreement and applicable government acquisition regulations.

(b) The audit program contains work steps and procedures on financial matters of interest to the foundation. The audit program should, in part, include:

- A determination of the adequacy of the accounting books and records;
- A review of the basic internal controls;
- Verification of expenditures of grant funds, reliability of expenditure reports submitted to the Foundation;
- Verification of Grantee or other party contributions to the grant project, if required by the grant agreement;
- An overall reconciliation of total funds received to project expenditures and available balances of funds;
- Sampling procedures used in the verification of expenses incurred during transaction testing;
- Audit procedures implemented for testing of individual transactions. The purpose of transaction testing is to determine, in part, whether costs are allowable, allocable and reasonable;
- Verification that no conflict of interests exists between the Grantee and the In-Country Service Provider, contractors or civil employees.

(c) Audit Periods

Certain Foundation grants call for interim audits to be made during performance of the grant project as well as a final audit upon completion of the project. In planning for an interim audit, unless otherwise specified in the grant agreement, the independent auditor will assure that the end of the interim audit period coincides with the end of report period in the latest expenditure report submitted to the Foundation as of the date of his visit. When a particular audit period is desired such as December 31 or June 30, the independent auditor should coordinate with the Grantee prior to his visit to assure that an expenditure report has been submitted to the Foundation as of the particular date.

For final audits, the end of the audit period will coincide with that of the final fiscal report submitted to the Foundation. In rare cases, for interim or final audits, it may be necessary for the auditor to construct the fiscal report based on his review of transactions. These cases would be due to administrative failures of grantees.

2. Audit Program Deviations

Although the audit program should be followed to the maximum extent practicable, the independent auditor is expected to determine those work steps under audit, and annotate his/her workpapers accordingly for later reporting to the Foundation. The independent auditor is expected to apply his/her professional judgment in determining the need for expansion of the examination beyond that required in the audit program, as appropriate when there is sufficient indication of a problem in a financial administration area.

In cases where the auditor considers that expansion of the examination beyond the programmed steps is needed, he/she should contact the Foundation's auditor to inform them of the area wherein expanded examination is considered necessary. Coordination between the independent auditor and the Foundation's auditor is considered essential not only for reaching a common understanding as to the importance of the expanded examination, but also to continually improve the audit program for additional work or approach that may be generally applicable to the Foundation's audit requirements.

3. Audit Procedures and Steps

Preliminary audit steps include analysis, evaluation and assessments of various accounting principles and methodologies used by the Grantee to record financial transactions. Analyze the adequacy of the Grantee's accounting records and related financial controls to determine whether the accounting records can separately define the financial transactions that pertain to the grant project as set forth in the grant agreement and budget. The analysis should be sufficient to conclude whether reasonable internal controls are in effect to ensure the safeguarding and proper expenditure of project funds.

Many Foundation grant projects also require contributions from grantee and or other sources, the accounting records should be capable of separately defining receipt and expenditure transactions for the project as they pertain to each source providing funds.

(a) Preliminary Audit Steps

- (1) Review the grant provisions for requirements. This should include any amendments to the grant agreement and the latest expenditure report submitted to the Foundation as of the date that the auditor begins his audit. The auditor should become familiar with the nature of the grant project, budgeted expenditures in the grant agreement, and content of expenditure reports prior to performing the fieldwork.
- (1) Develop steps and procedures for transaction testing.
- (2) Throughout the course of the audit, document any identified risk indicators and your response/action to the identified risks. If no additional steps are required, or no risk indicators are identified, document this in the audit program and workingpapers.
- (3) Hold an entrance conference with the Grantee.

(b) Risk Assessment

Perform a risk assessment considering the following elements:

- (1) Materiality of claimed grant project cost;
- (2) Analyze over/under budgeted vs. actual cost elements;
- (3) Acceptability of accounting system and internal controls;
- (4) History with the Grantee;
- (5) Conflict of interests between Grantee, contractors, consultants and In-Country Service Providers (ICS).

The assessment of risk due to fraud is a cumulative process that (i) includes a consideration of risk factors individually and in combination, and (ii) should be ongoing throughout the audit. In determining Grantee compliance with laws and regulations, government auditing standards require auditors to design audit steps and procedures to provide reasonable assurance of detecting errors, irregularities, abuse or illegal acts that could (1) have a direct (or indirect) and material affect on the Grantee's financial representations or (2) significantly affect the audit objectives.

Auditor should also exercise (1) due care in planning, performing and evaluating the results of audit procedures and (2) a proper degree of professional skepticism to achieve reasonable assurance that material unlawful activities or improper practices are detected. Under the concept of professional skepticism, the auditor neither assumes that management is dishonest nor assumes unquestioned honesty. Rather the auditor recognizes that conditions observed and evidential matter obtained, including information from prior audits, need to be objectively evaluated to determine if Grantee financial representations are free of material misstatement.

(c) **Analytical Procedures**

Analytical procedures should include:

- (1) Based on the data obtained in the preliminary audit steps, prepare a Chronology of Significant Events.
- (2) Use the results of the risk assessment and analytical procedures to determine the nature and extent of transaction testing of major cost elements.

(d) **Internal Controls**

Ascertain whether or not the Grantee has reasonable internal controls in place over the safeguarding and expenditure of project funds. Verify that the Grantee has the following procedures in place:

- (1) Competent personnel with appropriately limited and clearly defined responsibilities in receiving and disbursing funds or access thereto;
- (2) Prior approval of expenditures by an appropriate individual in authority over the grant project; and
- (3) Adequate documentation such as invoices, receiving reports of supplies or equipment purchased to support expenditures claimed. Adequate documentation to support work and or travel expenses for payments made to individuals;

(e) **Field Work**

- (1) Make a general review of the accounting system and financial controls employed by the Grantee.
- (2) Determine whether the accounting system can identify:
 - Individual receipts, and the total amount of funds received from the Foundation separately;
 - Individual expenditures, the total amount of funds expended on project resources by budget line item and or category;
 - The amount of unexpended funds;
 - The balance of project funds and resources due from the Foundation;
 - Ascertain whether the Grantee has established internal controls over the safeguarding of assets and expenditure. Determine if prior approval of expenditures by appropriate individuals in authority exists; and
 - Determine if documentation such as invoices, receiving reports, etc. are maintained to support expenditures.

(3) **Petty Cash**

Verify that the Grantee has appropriate safeguards in place. If disbursements are made through petty cash, verify that the fund is adequately safeguarded under the control of a single authorized individual. Verify that approval and documentation support is a required procedure and that they are in use.

(4) **Accounting and Financial Controls**

- Bank accounts – verify that bank accounts used for grant transactions are reconciled monthly.
- Analyze and summarize all interest earned with project funds.

- Assets – Verify that subsidiary records or files are maintained to properly control the assets. These include projects involving accounting for various assets such as loan receivables under revolving loan projects and inventories of materials and equipment under construction projects. Verify that these records are reconciled periodically and that physical inventories of materials and equipment are taken periodically to assure the accuracy of the records.

5. Expenditures

The audit includes a review of expenditures of Foundation grant funds including loans made from revolving loan funds for determining:

- (a) Foundation Grant Funds
 - Verify the need and propriety of the expenditure under the terms of the grant agreement and grant budget schedule.
 - Accounting Records
- (b) From the Grantee's accounting records, review and document the total amount of expenditures recorded for the grant as of the expenditure report date in US dollar value.
- (c) Verify the reasonableness of the amount of significant expenditures such as those for land, property and equipment. These procedures require a physical verification of the land, property and equipment that may have been purchased and a review of the accuracy of the Grantee's expenditure reports furnished the Foundation. (Foundation's grant agreements generally provide that the Grantee will furnish a report of expenditures **and** requests for additional disbursement subsequent to the initial disbursement by the Foundation.)

- (d) Verify through reconciliation the total amount of expenditures claimed by the grantee as of the expenditure report date. This should be reported in U.S. dollars and in the local currency. The total expenses claimed by the Grantee should be presented in the audit report as a Schedule by applicable budget categories provided in the grant agreement.
- (e) Any expense category not falling within the budget category should be separately shown and identified accordingly.
- (f) Budget categories having \$1,000 (U.S. dollars) or more require transaction testing equal to 80 percent of the U.S. dollars.
- (g) In the case of a revolving fund from which numerous small loans may be made, the 80 percent need not apply. However, an initial random sample may be taken, and if no exceptions are noted, additional transaction testing may be randomly made in order to meet statistical sampling requirements. The auditor will use his/her professional auditor judgement. He/she should document the rationale for any conclusions reached in his workpapers as support documentation.
- (h) Revolving Loan Fund

For grants having a revolving loan fund component, verify receipt of loan funds. A 50 percent of the value of the fund should be verified through transaction testing. This will be determined based on the independent auditor's risk assessment and other audit factors. If loans are numerous, the random and judgmental selection should be based on the risk assessment, prior audit (if any) of the Grantee.

Confirmation may be made through mail or visits to the major borrowers. If verification cannot be made through mail, a personal visit to major borrowers will be required to confirm the loans.

Expenditures, including loans made from revolving funds, will be audited and reviewed to assure that:

- Examine the status of loans and repayments to determine whether there are delinquency problem;
- Verify and report on the total outstanding loans considered delinquent;
- Verify and report on the total outstanding loans considered as uncollectible;
- Examine the utilization of loan recoupment for compliance with the intent for the grant agreement; and
- Furnish a summarized statement on the receipt, application and balance of the loan fund as of the audit date. Separately identify any delinquent and uncollectible loans.
- Expenditures were necessary and proper in accordance with the terms and conditions of the grant agreement and budget schedule;
- Advances included in grantee expenditures should be reported if outstanding for inordinate periods;
- Advances comprising of substantial portion of a particular expense category total should be noted in the audit report and related schedules;
- Verify that expenses were approved by an individual in authority over the grant project and are supported by appropriate documentation;

(i) Purchasing Procedures

- Review the Grantee's purchasing policies and procedures to ascertain that the Grantee has in place appropriate steps to determine that reasonable and competitive prices are obtained from vendors. In analyzing whether the Grantee has reasonable policies and procedures in place, consider the following:
- The policies and procedures include price checking in applicable manufacturer's catalogs and price lists;
- The policies and procedures includes obtaining competitive price quotations from reputable sources;
- Prices paid should not exceed what is charged other customers for similar items and quantities on similar terms;
- Where land is purchased, a survey of the market area should be conducted (through several sources) to ascertain whether the price paid is with current market prices;
- Physically inspect items costing over \$1,000. These include land, property and equipment;
- Determine whether purchases are approved at an appropriate management level;
- Ascertain that the Grantee's purchasing policies and procedures has adequate controls to prevent the unauthorized purchases; and
- Where the grant agreement specifies a price limit for the purchase of land, property or equipment that price should not be exceeded. However, the applicability to determine the reasonableness of the price below any ceiling limits is applicable regardless of grant agreement ceilings.

The Grantee should organize and administer the purchasing department to ensure the effective and efficient procurement of required quality materials and parts at the most economical cost from responsible/reliable sources.

(e) Budget Line items

For each expense budget line item having an equivalent U.S. dollar value of \$2,500 or less, examine through transaction testing at least five randomly selected transactions for detailed audit. This nature and extent of the transaction testing in this area will be determined based on the risk assessment conducted by the auditor during the preliminary audit. The auditor must document in the workpapers any conclusions reached as a result of the risk assessment and the basis for the transaction selection.

- In addition to the transaction testing physically inspect several items costing under \$1,000. These may include land, property and equipment for which support documentation was verified;
- Ascertain that the asset(s) is identifiable as Grantee property;
- The asset(s) are being used for the grant project;
- The asset(s) are being reasonably protected and cared for; and
- The Grantee has the assets under some form of property record and or accounting control so that the Grantee can satisfactorily account for all individual assets.

(f) Related Third Parties

Follow-up on large payments to third parties related to the grantee's project effort. (This includes loans and advances.)

Review expenditures and or use of funds by third party to the extent necessary to assure propriety of expenditures with the intent of the basic grant agreement.

Using the latest expenditure report submitted to the Foundation by the Grantee, reconcile to the audited expenditures as contained in the accounting records of the Grantee's as of the expenditure report date. Include a comparative analysis of the expenditure report and the audited expenditures as of the expenditure report date. The two should coincide with the audit period.

4. **Other Party Contribution to Grant Project**

The audit includes a review to determine whether the Grantee has complied with his/her obligation to contribute or obtain funds or other resources for the grant project in accordance with the provisions of the grant agreement. To ascertain whether the Grantee has made an attempt to obtain any contributions from other sources if required or provided by the grant agreement.

During the preliminary audit steps, as noted above, the auditors should have obtained a copy of the grant agreement, including any and all amendments, and reviewed the basic grant agreement for any provisions setting forth:

- (a) The unequivocal obligation of the Grantee to contribute his funds or other resources to the grant project and value thereof.
 - Determine whether or not the Grantee has met his/her obligation as of the audit date according to the time frame established in the grant agreement;
 - Examine and verify the expenditure or use of contributed funds or application of other resources to the project as necessary to assure compliance with the grant agreement
- (b) The unequivocal obligation of the Grantee to obtain contributions from other sources such as matching funds, and the amount thereof.
 - Determine whether or not the Grantee has obtained contributions as of the audit date in accordance with the time frame established for obtaining the contributions.

- Examine and verify the expenditure or use of contributed funds or application of other resources to the project as necessary to assure compliance with the grant agreement.
- (c) The obligation of the Grantee to attempt to obtain contributions from other sources.
- Determine whether or not the Grantee has made an effort as of the audit date to obtain the contributions in accordance with the time frame and other conditions established in the grant agreement.
 - For any contributions obtained, examine and verify the expenditure or use of funds or application of other resources to the project as necessary to assure compliance with the grant agreement.
- (d) Any time frame for making, obtaining, or attempting to obtain the contributions.
- Ascertain whether the Grantee has complied with this requirement.

When the performance of an audit occurs prior to any time frame established for making, obtaining or attempting to obtain a contribution to the grant project, the auditor should report this fact in **general comments** of the audit report.

Where the grant agreement does not specify a time frame for making, obtaining or attempting to obtain a contribution, the auditor should use his/her professional judgement as to the Grantee's compliance as of the audit date in context of the grant agreement, phasing of project work (requiring the resources to be contributed) and duration of the grant agreement with the Foundation.

5. **Reconciliation**

The auditors should reconcile the total funds received for the project to project expenses and available fund balances. This will ensure that all funds received for the project are accounted for either in their application to the project or in an unexpended balance available for project use. The reconciliation should include the total amount of funds received from the Foundation and from all other sources. The reconciliation should include amounts by budget line items showing total available funds, total expended funds and the unexpended available funds (these should be shown by line item). The audit should include the following:

- (a) Verify the cumulative amount of funds received by the Grantee. This includes funds from the Foundation and any other sources as of the end of the audit period;
- (b) Verify and analyze the cumulative amount of funds expended or used on grant projects as of the end of the audit period. Do not include as expense any allocation of expenses to the project which did not involve an actual disbursement of funds received for the project. However, they should be identified as such in a footnote.
- (c) Calculate the total amount of unexpended funds available for the grant project on deposit or on hand in the Grantee's depositories. (If funds provided by the Foundation have been co-mingled with other funds, ascertain and verify that accounting records can appropriately define and separate transactions and amounts from other sources.

Complete an analysis of the amount of funds available for grant projects and the amount of funds expended on grant projects with the cumulative amount of funds received. If the analysis shows that the funds available and funds expended on grant projects is less than the funds received the misapplication of funds should be discussed with the Grantee to obtain the facts and circumstances.

The matter, including the amounts involved and discussions with the Grantee should then be reported to the Foundation in accordance with this audit guidance.

Interest payments on loans from revolving loan funds must be adjusted out of the funds on hand or on deposit to calculate audit steps (b) and (c) above. Any outstanding loans should be considered as expenses since recoupment of principle or prior loans should have formed part of the cash balance for the revolving loan fund.

6. **Concluding Audit Steps**

(a) **Summary**

Summarize the results of audit of individual grant requirements and individual cost elements. Assess whether any significant over/under budget costs require further pursuit or referral because the audit detected material errors, irregularities, abuse or illegal acts. Do not release or disclose to the Grantee information relating to a matter referred for investigations. Immediately contact the Foundations auditor with the details and any recommendations.

(b) **Exit Conference**

Hold an exit conference with the Grantee documenting the name of the Grantee or Grantee representative and date of exit conference. Document any discussions relative to the audit conclusions that the Grantee may have responded to. Confirm and or follow-up on requests for the Grantee's reaction to any audit exceptions for inclusion in the audit report. The auditors, when possible, should obtain a written response from the Grantee on issues requiring the Grantee to comment on audit findings. This written response should be included in the audit report as an attachment.

Document the exit conference in the working papers including dates, participants, names and titles and specifically discussed items. Note the Grantee's reactions, if any. This provides the information to be included in the audit report.

(c) **Audit Report**

Prepare the audit report. Assure the notes sufficiently explain and support conclusions. The report should include information on the exchange rate of the local currency as of the last day of the audit period covered. Information on the exchange rate at the time of disbursement should also be provide.

7. **Schedules:**

- (a) Provide a schedule showing the various costs by line item. The schedule should include the budgeted amount compared to actual costs for the period of the audit. (See attachment.)

G. **Sample Audit Report**

Audit Report format and contents – To satisfy government-reporting standards, there must be a written record of each audit. Issuing an audit report satisfies this requirement.

EXAMPLE

[Cover Sheet]

PREPARED FOR: Inter-American Foundation
901 N. Stuart Street
Arlington, VA 22203

PREPARED BY: Juan Del Pueblo Y Asociados
Contadores Publicos
123 Calle del Gallo
Quito, Ecuador
Teléfono No. 1234 5678
FAX No. 2345 6789
E-mail Jdoe@yahoo.com

SUBJECT: Report on Audit of Grant EC-999
1 March 1998 through 28 February 1999

GRANTEE: Proyecto del Sol
456 Avenida de los Contadores
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Teléfono No. 9876 1234
FAX No. 8765 4321
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Grantee Organization and Systems	x

E X A M P L E

Subject of Audit

[This section should identify the period audited, the purpose of the audit and the Grantee to which the audit applies. It should include the period covered under the audit. This section should also include the total grant dollars audited in both U.S. dollars.]

[Example]

We audited the [Grantee's Name] books and records for compliance with requirements described in grant agreement no. [EC- 999] dated March 10, 19XX and applicable amendments for a total of \$99,800 in U.S. dollars. Our audit covered the period of March 10, 19XX through September 30, 19XX.

The Grantee's financial records, related supporting data and compliance with the requirements described in the grant agreement are the responsibility of the Grantee. Our responsibility is to express an opinion based on our audit.

Executive Summary

This section gives a brief overview of the audit findings. It briefly describes the audit opinion, recommendations and the significant issues supporting the opinion. The Executive Summary should rarely exceed one page. This section can be omitted if the report has no audit findings.

[Example]

Our audit of [Grantee's] books and records disclosed several deficiencies and weakness including the following significant items:

Contributions to the Project

- The Grantee had committed \$70,000 in contributions to the Project by 15 July 1999. As of this date, the Grantee has contributed \$50,000.

EXAMPLE

Equipment

- The Grantee purchased \$15,000 in computer equipment that was not authorized by the grant agreement.
- The Grantee has exceeded the Budgetary Line Item 1, Salaries by \$18,000. This represents a 30 percent increase over the approved budget.

Materials

- We tested a total of \$30,000 in material purchases representing 25 transactions. The Grantee could not provide support documentation to 7 of these transactions representing \$10,000.

SIGNIFICANT ISSUES

1. The Grantee has not contributed \$70,000 as required by the grant agreement.
2. The Grantee has purchased equipment not authorized by the grant agreement.
3. The Grantee has exceeded a budget line item in excess of 30 percent. The Grantee has not obtained authorization as required by the grant agreement.
4. No support documentation was provided for \$10,000 of purchased items.

This section describes any significant issues as described above.

Scope of Audit

Except for the qualifications discussed below (*omit if there is no "Qualifications" section within the "Scope" paragraph*), we conducted our audit in accordance with generally accepted auditing standards issued by the American Institute of Certified Public Accountants and with generally accepted government auditing standards issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain a reasonable assurance about whether the data and records are free of any material misstatement. An audit includes

1. Reviewing the Grantee's internal controls, assessing control risk, and determining the extent of audit testing needed based on the control risk assessment;
2. Examining, on a test basis, evidence supporting the amounts and disclosures in the data and records reviewed;
3. Assessing the accounting principles used and significant estimates made by the Grantee;
4. Evaluating the overall data and records presentation; and

5. Determining the need for technical specialist assistance [and quantifying the results of a government technical evaluation].

EXAMPLE

[If auditing standards other than those of the American Institute of Certified Public Accountants (AICPA) were used, identify those standards and the issuing body of those standards.]

We evaluated the Grantee's books and records using the cost principles contained in the

1. Federal Acquisition Regulation (FAR) if applicable.
2. Industry or Technical Guides. [Identify any applicable guides actually used.]
3. Grant agreement Provisions.
4. Guidelines and Procedures required by the Inter-American Foundation.

[The scope of audit should also briefly describe the current status of the Grantee's accounting system and any other management systems which are used to control and account for the recording of costs; the current assessment of control risk and any other outstanding systems deficiency.]

GRANTEE'S INTERNAL CONTROL STRUCTURE

The Grantee's accounting system is considered adequate *[or inadequate as the case may be]* for the accumulation and reporting of costs incurred under the grant agreement. In our opinion, the *[Grantee's name]* internal control structure does not provide for assessing the control risk at less than the maximum and a reduction in substantive testing requirements. The Grantee is a medium sized *[or small sized as the case may be]* business that has limited resources to be applied to compliance procedures and testing. The Grantee does not conduct independent checks of compliance with government laws and regulations. Accordingly, we did not expand our audit effort to determine the extent to which we can rely on the Grantee's internal controls and their effect on our substantive testing. Our audit scope reflects this assessment of control risk and includes expanded testing of the Grantee's claimed costs to provide a reasonable basis for our opinion.

EXAMPLE

Qualifications:

[Describe and identify any circumstances, which may have a significant adverse effect on the audit or results. However, This paragraph would only include circumstances that have a material impact on the conduct of the audit and its results. Briefly describe, if any, each qualification including the impact the qualification had on the scope and results of audit. Specifically reference the report page number, exhibit, schedule or appendix paragraph that contains the detailed discussion on the item involved. The qualification section itself must state the adverse impact clearly and concisely and provide an estimate of its magnitude.]

Some additional items that may be noted in the qualifications paragraph include but not limited to:

1. Lack of access to the Grantee's books and records including budgetary data.
2. Time limitations on the scope of audit.
3. Deficiencies which render the accounting system inadequate and unreliable.
4. Internal reorganizations that are significant to the project that the effect on the project cannot be reasonably determined but is expected to be material.

Results of Audit

Audit Opinion

a. The auditor's opinion can be categorized in one of the following three areas:

1. Complete compliance (adequate),
2. Generally complied except for some minor deficiency (inadequate in part), or
3. Not in compliance (not adequate).

[Example – Unqualified Opinion on compliance with no significant audit findings.]

In our opinion, [Grantee's Name] complied, in all material respects, with the requirements of the grant agreement.

[Example – Unqualified Opinion on compliance – No significant audit findings noted; however, noncompliance with one or more requirements exist.]

In our opinion, [Grantee's Name] complied, in all material respects, with the requirements of the grant agreement. However, our audit disclosed instances on noncompliance with those requirements [identify relevant compliance requirements], which are required to be reported in accordance with the requirements of the Inter-

American Foundation [or other contract, laws and regulations] and are described in the accompanying Schedule of [name the schedule used], Appendix 1.

[Example – Qualified opinion on compliance –Scope limitation with no significant audit findings, modify as appropriate.]

In our opinion, except for the lack of access to budgetary data, as discussed in the qualifications section of this report, [Grantee's Name] complied, in all material respects with the requirements of the grant agreement. As discussed above, we excluded the review of the Grantee's budget data from our audit of compliance. Therefore, our audit opinion does not cover this Grantee data.

[Example – Qualified opinion on compliance – Significant audit findings and noncompliance with one or more requirements.]

In our opinion, except for those instances of noncompliance with the requirements that are applicable to the grant agreement [Grantee's name] complied in all material respects, with the requirements of the grant agreement. Our audit disclosed instances of noncompliance with the following requirements [identify relevant compliance requirements] that are applicable to the project development program [if applicable, list programs]. These noncompliances are described in the Schedule [name of schedule] Appendix 1. Compliance with these requirements is necessary, in our opinion, for [Grantee's name] to fully comply with the requirements applicable to the grant agreement.

Detail the major findings in the audit in this paragraph. The Results of Audit section of the report should contain all exhibits and supporting schedules required for a clear, complete presentation of the audit results.

EXAMPLE

BUDGET

(Equivalent in United States dollars - two year)

<u>Budget Line Item</u>	<u>IAF</u>	<u>XYZ</u>	<u>ABCD</u>	<u>Total</u>	<u>Notes</u>
1. Salaries					
a. Superintendent of Project	\$2000	\$1000	\$500	\$3,500	
b. Project Manager	500	250	250	1,000	
c. Administrative	200	150	150	500	
2. Equipment					
a. Computers	60,000	10,000	5,000	75,000	1
b. Software	5,000	5,000	1,000	11,000	
3. Materials					
a. Paper	2,000	1,000	1,000	4,000	
b. Diskette Back-up Drives	3,000	1,000	1,000	5,000	
4. Administration					
a. Office Space		15,000		15,000	2
b. Phones/FAX		3,000		3,000	
c. Furniture		2,000		2,000	
5. Dissemination & Gathering					
a. Communications (information gathering)	2,100	500	400	3,000	
6. Training					
a. Specific Training Classes (40 Members)	15,000		4,000	19,000	
b. Specific Technical Training	10,000	2,000		12,000	
TOTAL:	<u>\$99,800</u>	<u>\$40,900</u>	<u>\$13,300</u>	<u>\$154,000</u>	

Notes:

Provide any relative information on the various budget line items. The notes can be omitted if deemed insignificant or if there is nothing to report.

The auditors should provide information on the exchange rate at the time of original disbursement and the exchange rate at the time of last day included under the reporting period. The exchange rate should be the actual exchange rates at those time frames and not a weighted average rate.

EXAMPLE

INCURRED EXPENSES

(Equivalent in United States dollars - two year)

<u>Budget Line Item</u>	<u>IAF</u>	<u>XYZ</u>	<u>ABCD</u>	<u>Total</u>	<u>Notes</u>
1. Salaries					
a. Superintendent of Project	\$500	\$ 100	\$	\$600	
b. Project Manager		50	150	200	
c. Administrative	50	50	50	150	
2. Equipment					
a. Computers	5,000	1,000		6,000	1
b. Software	500	500	1,000		
3. Materials					
a. Paper	400	200		600	
b. Diskette Back-up Drives	500	400	100	1,000	
4. Administration					
a. Office Space		1,200		1,200	
b. Phones/FAX		300		300	
c. Furniture		500		500	
5. Dissemination & Gathering					
a. Communications (information gathering)	1,000		100	1,100	
6. Training					
a. Specific Training Classes (40 Members)	5,000		1,000	6,000	2
b. Specific Technical Training	2,000	300		2,300	
TOTAL:	<u>\$14,950</u>	<u>\$4,600</u>	<u>\$1,400</u>	<u>\$20,950</u>	

Notes:

Provide any detailed information relative to the budget line items. This may include information on expenses incurred for unauthorized items not within the grant agreement. It may include information deemed significant on budget line items that have been exceeded.

EXAMPLE

Funds Disbursed

(Equivalent in United States dollars - two year)

<u>Budget Line Item</u>	<u>IAF</u>	<u>XYZ</u>	<u>ABCD</u>	<u>Total</u>	<u>Note</u>
a. Cash Received Prior Period:	\$ 0	\$ 0	\$ 0	\$ 0	
Interest Earned Prior Period:	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	
Total Received Prior Period:	\$ 0	\$ 0	\$ 0	\$ 0	
b. Cumulative Expense Prior Period:	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	
c. Cash on Hand:	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>	
Add:					
d. Cash Received This Period:	\$50,000	\$20,000	\$13,300	\$83,300	1
Interest Earned This Period:	<u>5,500</u>	<u>2,000</u>	<u>1,000</u>	<u>8,500</u>	2
Total Received This Period:	\$55,500	\$22,000	\$14,300	\$91,800	
e. Cumulative Expenses This Period:	<u>14,950</u>	<u>4,600</u>	<u>1,400</u>	<u>20,950</u>	3
f. Available Cash on Hand:	<u>\$40,550</u>	<u>\$17,400</u>	<u>\$12,900</u>	<u>\$70,850</u>	4

Note:

1. Provide any relevant information on the funds received by the Grantee. This note can be omitted if deemed insignificant.
2. Provide information on they type of bank account used by the grantee. Information should include whether the funds are maintained in U.S. dollars or in current local currency. If this item includes other earnings, show the composition of these amounts.
3. Provide any relevant information on actual expense that has exceeded the budget line item or expenses not authorized by the grant agreement.
4. Provide any relevant information that is deemed significant on available funds. This may include excess funds not being utilized by the Grantee. This note can be omitted if deemed insignificant.

The auditors should provide information on the exchange rate at the time of each original disbursement and the exchange rate at the time of last day included under the reporting period. For the calculation of any remaining unused funds, the exchange rate should be the actual exchange rate on the first day after the end of the grant agreement and not a weighted average rate.

EXAMPLE - Continued...

The audit report results were provided and discussed with [*name and title*] on [*date*]
[*outcome*]

Statement of Condition and Recommendation

[The statements of condition and recommendation are an integral part of the results of audit and should follow the narrative described in the Results of Audit. Alternatively, they may be included in attached appendixes.]

Grantee's Organization and Systems

This section should furnish pertinent information necessary for the reader to understand the area reviewed.

1. Organization

[In this section, provide information relative to the Grantee. This should include information on when the organization was established, the purpose and objectives of the organization, size of organization, and any other pertinent information about the organization. Include information about the project such as dates, milestones, expected outcome of the project, etc.]

2. Accounting System

(Provide a brief overview of the Grantee's accounting system. This should include how the Grantee accounts for various contributions or donations by other organizations, how costs are recorded, accumulated and identified. This may include information on whether the Grantee has a manual accounting system or computerized accounting system. Provide any relevant information.)